

DEPARTMENT OF DEFENSE GUIDANCE FOR PRIVATIZING DEFENSE UTILITY SYSTEMS

I. PURPOSE

Privatization allows installation commanders to focus on core defense missions and functions by relieving them of activities that can be done more efficiently and effectively by others. DRID 49 directed Defense Components to privatize every government owned electric, water, wastewater and natural gas utility system unless security concerns required federal ownership or privatization was uneconomical. Historically, military installations have been unable to upgrade and maintain reliable utility systems fully due to inadequate funding and competing installation management priorities. Utilities privatization is the preferred method for improving utility systems and services by allowing military installations to benefit from private sector financing and efficiencies.

Based on lessons learned and the utilities privatization plans submitted by the Military Departments, this document replaces DRID 49 and updates guidance for conducting the economic analysis necessary to make a determination to privatize. It also clarifies the role of state laws and regulations as the Defense Components use competitive procedures in these efforts.

II. SCOPE

A. DEFINITIONS

Key terms used in this guidance are defined in *Appendix A*.

B. DIRECTIVE

The Under Secretary of Defense (Acquisition, Technology and Logistics) (USD(AT&L)) shall oversee utilities privatization program execution to maintain effective progress, including review of utilities privatization strategic master plans, quarterly status reports, and acquisition plans, as necessary. USD(AT&L) shall develop broad policies and procedures necessary to execute the program, including economic analysis tools and recommended legislative and regulatory changes. USD(AT&L) shall establish a Utilities Privatization Working Group, chaired by the Director, Utilities and Energy Use, Office of the Deputy Under Secretary (Installations and Environment) (ODUSD(I&E)) and composed of representatives from all Military Departments and affected Defense Agencies, to achieve efficient and effective program implementation through communication, consistency, codification and standardization.

Using this guidance, by September 30, 2005 the Defense Components shall complete a privatization evaluation of each utility system at every Active Duty, Reserve, and Guard installation, within the United States and overseas, that is not designated for closure under a base closure law. This milestone is satisfied when the Source Selection Authority (SSA) makes a decision or the Defense Component submits an exemption.

The utilities privatization initiative is a large one-time workload of developing numerous RFP packages and evaluating over 1500 systems. Following an initial evaluation with no award, Components may re-evaluate a system. At least the initial evaluation shall be complete on all systems by September 30, 2005.

In circumstances in which a Defense Agency operates an installation under the jurisdiction of a Military Department; the Director of that Defense Agency shall conduct the utilities privatization process on behalf of the Secretary concerned. However, in all cases, authority to convey a utility system and to enter into a utility service contract under Section 2688 of Title 10, United States Code (10 U.S.C. 2688), remains with the Secretary concerned.

To achieve innovative results, privatization must proceed in a deliberate manner that promotes industry interest and competition to the maximum extent practical. Components have recently developed revised master plans to reflect lessons learned. Within two weeks following receipt of this guidance, the Components shall submit to USD(AT&L) a detailed schedule of projected progress to support their master plan. The schedule shall be updated annually on September 30 through the completion of the program. The Components shall submit quarterly status reports to DUSD(I&E) that compare actual progress to the planned schedule and provide comments explaining deviations. The Utilities Privatization Working Group shall determine the format of the submission and quarterly updates.

Components shall quantify the requirements for utility privatization and any shortfalls in meeting these requirements in their annual program and budget submissions to OSD.

Based on the initial Component master plans, this guidance establishes the following draft interim milestones:

- By October 15, 2002 the DUSD(I&E) will issue final interim milestones for each Component.
- By September 30, 2003 close Requests for Proposals (RFPs) or submit certificates of exemption on at least 80 percent of a Component's utility systems available for privatization.
- By September 30, 2004 reach Source Selection Authority decisions or submit certificates of exemption on at least 65 percent of a Component's utility systems available for privatization.

The interim goals should not discourage procurement officials from adjusting RFP schedules to accommodate efforts to maximize the number of systems privatized.

Per Section III, the Secretary concerned may exempt some systems from privatization as defined by this guidance. In the event the Secretary concerned certifies the basis of an exemption, the Component is encouraged to pursue other innovative measures to improve operational efficiency. Such measures may include competitive sourcing, developing solicitations combining system operations and maintenance and energy conservation investment programs, or partnerships with the General Services Administration or other agencies.

C. AUTHORITY

Privatization normally involves at least two transactions with a successful offeror: (1) conveyance of the utility system; and (2) acquisition of utilities services for a long-term commitment of up to 50 years (10 U.S.C. 2688(c) (3), as amended).

1. Conveyance of the Utility System

10 U.S.C. 2688 authorizes the Secretary concerned to convey a utility system to any municipal, private, regional, district or cooperative utility company or to any other entity. In order to effectuate privatization of the utility system (as opposed to outsourcing utility system operation and maintenance) the Military Department must convey all rights in the asset. While leasing alone is not sufficient to transfer ownership, if the Secretary concerned determines that delayed transfer of title is economically preferable to an immediate transfer of title, the Secretary may structure the conveyance as a lease-purchase or a lease in furtherance of conveyance, as long as the non-federal entity at some point takes title to the asset. In the case of overseas utility systems, privatization must also comply with applicable international agreements and host nation laws.

As explained in greater detail in the legal opinion from the General Counsel of the Department of Defense at *Appendix B*, state laws and regulations are not applicable to the conveyance of a utility system under 10 U.S.C. 2688. Although Section 2813 of the Floyd D. Spence National Defense Authorization Act for Fiscal Year 2001 (Public Law 106-398) amended Section 2688 after the General Counsel issued the legal opinion, the amendments do not alter any of the conclusions of that opinion. Additionally, traditional Federal real property disposal laws and regulations (e.g. McKinney Act, Federal Property and Administrative Service Act, etc.) do not apply to the disposal of utility systems under 10 U.S.C. 2688.

The authority to dispose of a utility system under 10 U.S.C. 2688 is contingent upon meeting two statutory requirements: (1) the receipt of fair market value, and (2) the Secretary concerned providing Congress with an economic analysis demonstrating for each individual utility system, that “(A) the long-term economic benefit of the conveyance to the United States exceeds the long-term economic cost of the conveyance to the United States; and (B) the conveyance will reduce the long-term costs to the United States for utility services provided by the utility system concerned”, 10 U.S.C. 2688(e)(1). To be conveyed, each individual utility system must meet these two statutory requirements. If either requirement is not met, the conveyance cannot proceed no matter how beneficial the Military Department may otherwise consider the privatization action. The Defense Components shall conduct the congressionally required economic analysis in accordance with OMB Circular A-94, DODI 7041.3, and Section IV of this guidance.

2. Acquisition of Utility Services

The provision of utility services necessitated by the conveyance of the utility system under 10 U.S.C. 2688 is an acquisition of services and is therefore governed by the FAR and its

supplements. As explained in greater detail in *Appendix B*, states may not regulate the Federal Government's acquisition of utility services related to the utility system conveyed under the authority of 10 U.S.C. 2688. Federal procurement laws and regulations take precedence and cannot be frustrated by the application of state or local laws. The Defense Components must comply with state laws and regulations only when acquiring the electricity commodity (Section 8093, Department of Defense Appropriations Act of 1988 (Public Law 100-202)).

The Defense Components should determine the length of the utility service contract pursuant to the FAR and its supplements. Relevant considerations include:

- The period of time required by the offeror to amortize its investment to acquire and upgrade the existing system;
- The life expectancy of the upgrades to be made by the offeror;
- The ability to obtain continued utility system service at a reasonable cost; and
- The possibility of using options to extend a utility service contract.

3. Requirements of the Purchaser

The purchaser of the utility system must be obligated, as a matter of contract, to ensure the provision of reliable utility service to the installation. The Defense Components shall ensure that the combination of utility services contract, easement, and real estate documents contain provisions to: (1) ensure proper performance to the level defined by the standard used to develop the government estimate of "should costs"; (2) in the event of default, abandonment or severe non-performance allow the Component to regain operational control of the system, procure alternative services, and collect reasonable reimbursement from the purchaser and (3) require the conveyee to manage and operate the utility system in a manner consistent with industry standards and the applicable Federal, state and local regulations pertaining to health, safety, fire, and environmental requirements. To minimize the risk to mission requirements in the event of non-performance, Defense Components shall include language in the contract and real estate documents that will permit a stepped approach to enforcement actions to protect the government's interest. Components may include reversionary clauses to provide for title in the system to revert to the Government only in extreme cases of non-performance such as an abandonment or bankruptcy with no provisions for continued services.

Purchasers of military utility systems are not required to comply with state licensing or similar requirements that would undermine the Federal competitive selection of an entity, impose a significant burden on the Federal Government, or conflict with a Federal system of regulation. However, as noted above, the contract for the conveyance must require the purchaser to manage and operate utility systems in a manner consistent with applicable federal, state and local regulations pertaining to health, safety, fire and environmental requirements.

Federal Taxes (including Contribution in Aid of Construction) contained in an offer shall be considered a wash cost in the economic analysis of that offer compared to the government should cost and in the source selection process. However, Components must ensure that proof of that tax liability be provided prior to making payments that include the contractor's federal tax costs.

III. EXEMPTIONS

The Secretary concerned may exempt a utility system from privatization when (1) unique mission or security reasons exist or (2) the privatization is determined to be uneconomical. In either case, the Secretary concerned shall certify, with justification, the basis for the exemption to the USD (AT&L).

A. UNIQUE MISSION OR SECURITY REASONS

A unique mission or security reason is a situation in which ownership of the utility system by a private utility or other non-Federal entity would (1) create an unacceptable risk of substantial impairment to the Military Department's mission, or (2) compromise classified operations or property.

B. UNECONOMICAL

Privatization is considered uneconomical only when there is a demonstrated lack of market interest, or when the costs to the Government exceed the benefits.

1. Lack of Market Interest

The Secretary concerned may exempt a utility system from privatization when there is a lack of market interest as demonstrated by no response from any qualified utility provider or other entity. In order to solicit maximum interest and participation, the Defense Components should publish Requests for Interest (RFIs) at the Government wide Point of Entry (GPE) that can be accessed via the internet at <http://www.fedbizzops.gov>. The proposed solicitation should also be advertised or announced in at least two other forms of relevant print or electronic media. Examples of relevant media include: mass mailings, the Internet, technical industry journals, trade association publications, national and regional publications, and state, regional, and local publications. If the Secretary concerned is convinced that sufficient interest and therefore competition exists, the Secretary may forego publication of an RFI and proceed directly to issue an RFP.

The Defense Components shall issue RFPs for all systems with expressed market interest in response to an RFI. The Defense Components shall synopsise all RFPs in the GPE to advertise the government's intent to privatize a utility system and advertise or announce the request in at least two or more other forms of relevant print or electronic media. If no responsible proposals are received, the local utility provider should be specifically requested to provide a proposal or feedback. If there are still no qualified responses to the RFP, the system may be exempted as uneconomical. Feedback on the lack of interest should be provided to the Utilities Privatization Working Group.

2. Costs Exceed Benefits

The Secretary concerned may exempt a utility system from privatization when, after evaluating all responses to the RFP, the economic analysis fails to meet the requirements of 10 U.S.C. 2688(e). The Defense Components shall compare the costs and benefits to the Federal Government on offers received in response to the RFP and conduct the economic analysis in accordance with Section IV. B. The potential offerors should be queried to determine if any significant barriers precluded government requirements from being met through privatization. Feedback on barriers shall be considered in further efforts to privatize the utility system. Pertinent feedback on the barriers should also be provided to the Utilities Privatization Working Group. If the system is still determined to be uneconomical, the exemption justification shall include the feedback along with the economic analysis.

IV. IMPLEMENTATION

A. SOLICITATIONS AND SOURCE SELECTION

If in response to an RFI, more than one entity expresses an interest in the conveyance of a utility system, 10 U.S.C. 2688 requires that the Defense Components dispose of the utility system using competitive procedures, notwithstanding state laws and regulations regarding who can own and operate a utility system. Congress, in authorizing utility privatization, did not surrender Federal supremacy, nor did it waive the sovereign immunity of the United States with respect to disposal. Therefore, any effort to dispose of the utility system in a non-competitive manner, when more than one entity expresses an interest in the conveyance, even if undertaken to voluntarily comply with state law, would violate the requirements of 10 U.S.C. 2688. Notwithstanding the requirement to compete if more than one entity expresses interest, the Secretary concerned may use procedures other than competitive procedures, but only in accordance with subsections (c) through (f) of Section 2304 of Title 10, United States Code, to select the conveyee. However, because the Military Department's disposal of utility systems is not subject to state law, regulation, or policy, the Military Department cannot use such laws, regulations, or policies as justification to enter into a sole source negotiation.

The Defense Components shall select a provider that best meets the utility service requirements of the installation and provides long-term benefits and reduced utility service costs to the United States. The Defense Components should develop strategic RFPs that enhance the Government's potential benefit and encourages maximum participation by the utility industry. Although each utility system must be analyzed separately for the purpose of the economic analysis required by 10 U.S.C. 2688, the Defense Components should consider strategically grouping multiple utility systems into a single solicitation to create economies of scale in utility service. Examples of characteristics to consider when doing so are: (1) market interest; (2) operational requirements; (3) financial factors; (4) environmental concerns and (5) geographic location. FAR 7.107 provides guidance on contract bundling.

1. Requests for Proposal

The Defense Components should consider standardization of RFPs to encourage broader participation in the solicitations. At a minimum, the Defense Components shall develop RFPs that:

- Ensure the solicitation process is conducted in a manner to ensure that all interested regulated and unregulated utility companies and other entities receive an opportunity to acquire and operate the utility system conveyed;
- Allow a minimum 120-day response period. Additional time may be required for RFPs containing multiple systems or complex issues;
- Use a standard past performance questionnaire similar to *Appendix C*;
- Contain a provision stating that the Military Department cannot guarantee that it will enter into a contract with the provider at the end of the proposal evaluation process, nor contract renewal at the end of an awarded contract period;
- Provide sufficiently detailed data and/or allow prospective offerors access to perform the due diligence necessary to prepare competitive proposals; and
- Address security concerns for releasing detailed base information to the public in the RFP process. Defense Components should consider methods to limit distribution of this information to bona fide offerors only, which have agreed to restrict its dissemination to authorized users.

When multiple systems are offered in a single solicitation, the Defense Components shall develop RFPs that:

- Allow interested entities to bid on individual systems, multiple systems, the entire package, and any alternative combination of systems, to ensure that all entities (regulated and non-regulated) have a fair chance in the competition; and
- Contain a provision requiring that all costs, including fixed costs that apply to all systems in the proposal, be allocated in a fair and reasonable manner to allow the Government to conduct the economic comparison of each individual utility system required by 10 U.S.C. 2688.

2. Source Selection Considerations

The Defense Components shall make a best-value determination, pursuant to the FAR and its supplements. Among the relevant considerations are:

- All qualitative (non-monetary) considerations, which are to be discussed in a narrative format as directed in DODI 7041.3; and,
- Other possible long-term costs and benefits to the United States, if the conveyance affects separate contract relationships, particularly for commodities.

An offer for multiple systems may present the best-value to the Government. If one or more of the individual systems contained in a multi-system offer does not satisfy the requirements of 10 U.S.C. 2688(e), but the multi-system offer when considered collectively does satisfy it, the Military Department should carefully review whether common costs are appropriately distributed to each individual system. If by properly adjusting the allocation of common costs, each utility system can be shown to be economic, then transactions for each system can proceed. Any conclusion that an individual system does not satisfy the economic analysis requirements is to be reviewed by the Acquisition Executive of the Military Department.

The purpose of this review is to ensure that the appropriate allocation is utilized. A copy of this review and the economic analysis shall be submitted with any economic exemption package submitted to USD(AT&L).

3. Fair Market Value

10 U.S.C. 2688(c) requires the recipient of the utility system to provide compensation to the Government for the fair market value (FMV) of the system as determined by the Secretary concerned. The Secretary concerned may accept this consideration in the form of a lump sum payment or a reduction in the charge for utility service provided by the conveyee. The Military Department shall handle a lump-sum payment in accordance with the procedures described in the DoD Financial Management Regulations. If the Secretary concerned elects to receive consideration through a reduction in the charge for utility services provided to the military installation, the length of time necessary to realize the reduction in charges shall not be longer than the life of the utility services contract.

The Military Department shall develop a range of FMV as part of its negotiation strategy to take into account the business and strategic values of the utility system. The Military Department may choose to determine FMV through an actual appraisal, a modified cost/income analysis, or a Replacement/Original Cost New Less Depreciation analysis.

B. ECONOMIC ANALYSIS

OMB Circular A-94, DODI 7041.3, and this guidance constitute the Department of Defense-approved life cycle costing procedures required by 10 U.S.C. 2688 to conduct economic analyses in support of utility privatization. The Defense Components shall use a benefit-cost analysis as described in OMB Circular A-94 to perform the economic analysis of each utility system, including net present value calculations to determine the life cycle costs and benefits of each proposal. To facilitate these calculations the Office of the Secretary of Defense (OSD) commissioned the development of the Utilities Privatization Economic Analysis Support Tool (UPEAST) to perform this benefit-cost analysis.

The Defense Components shall use the discount rate expressed in either real or nominal terms, issued annually by the Under Secretary of Defense (Comptroller) pursuant to DODI 7041.3. Generally, economic analyses should use the real discount rate. If future benefits and costs are proposed in nominal terms, then the nominal rate shall be used. Real and nominal values shall not be combined in the same analysis.

1. Economic Analysis Methods

The Defense Components shall utilize the UPEAST analysis model found at <http://www.acq.osd.mil/installation/utilities/privatization.htm> or a comparable cost model to conduct the required life cycle cost analysis. UPEAST will continue to be developed by DUSD(I&E) using lessons learned from the Utilities Privatization Working Group. Prior to

submitting to DUSD(I&E) for determining comparability, the Defense Components shall ensure any comparable cost model:

- Assumes a General and Administrative rate of 25% on Government O&M labor costs. This factor is based upon the percentage of the historical annual cost of O&M (adjusted) “should cost” that is directly attributable to Government labor exclusive of direct labor;
- Assumes a Contract Administration rate of 5% of adjusted total O&M costs;
- Measures cost and benefits to the United States such that it requires that all Federal taxes (including Contribution in Aid of Construction) contained in an offer are credited back to the offeror; and,
- Assumes a Transition Cost of 10% of the O&M labor costs, with a \$50,000 maximum cap.

The above rates are established as initial DoD-wide standards and will be updated periodically to reflect more accurate rates as they become known through program performance. The use of other than the above G&A, contract administration and transition cost rates must be justified and documented fully in the economic analysis.

The Defense Components shall consider the cost to transfer the utility system to the new owner (including initial monitoring and the cost of reduction and or displacement of personnel) as transition costs and shall include these costs in the Government’s life cycle cost analysis. The Defense Components shall consider implementation costs as sunk costs and should not include them in the Government’s life cycle analysis. See *Appendix A* for definitions.

Non-monetary and environmental considerations can be significant factors in the economic analysis. The Defense Components shall establish a ranking or weighting summary for these considerations and, at a minimum, document them in a narrative format as directed in DODI 7041.3. Conversely, factors that may result from the correction of deferred maintenance and functional deficiencies such as quality of life benefits shall be considered as “wash costs”.

By transferring ownership the government also transfers the risks associated with that property. Liability for a variety of potential negative situations would be transferred to the new owner, who should be better able to manage the risk. Although the government is self insured, this transfer of risk has some value depending on various factors. In conducting the economic analysis Components shall consider the reduced risk.

The period of analysis of the congressionally required economic analysis shall be at least as long as the anticipated utility service contract. The utility service contract, in conjunction with the conveyance of a utility system (10 U.S.C. 2688(c)(3), as amended), including any option(s), may be for a maximum length of up to 50 years. If cost elements change during negotiations, the Military Department shall update the economic analysis to accurately demonstrate whether privatizing the utility system under the terms of the anticipated utility service contract will meet the requirements of 10 U.S.C. 2688. This economic analysis shall accompany the notification package that is forwarded to USD(AT&L) and Congress.

2. Installation and System Assessment

The Defense Components shall conduct installation and utility system assessments to fully identify “should costs.” The Defense Components should review standard industry cost elements when determining “should costs” to ensure a meaningful calculation of Government “should costs” relative to bid proposals. The Defense Components shall use surveys and questionnaires to fill data gaps in the assessments. The Defense Components shall identify, as comprehensively as practicable, all activities and associated costs of operating and maintaining the utility system at a “should cost” level.

In developing “should costs”, it is important to capture all direct, indirect labor, material and equipment associated with the system. During the assessments, the Defense Components shall give special attention to identify all installation functions that should provide peripheral support (personnel and equipment) to the overall long-term operation and maintenance of each utility system. If the conveyance of the utility system would either reduce the costs for such peripheral support, or identify personnel or equipment resources available for other purposes that could benefit the installation, then the peripheral support costs must be included in the analysis.

The following resources form the basis of the assessments: installation planning and program documents (i.e., 5-year budget plan), the most recent as-built and other construction drawings, shop and maintenance records, contract records, and personal interviews. The system assessment will identify the location, components, materials, and condition of the system and those costs associated with all deferred maintenance, physical and functional deficiencies and areas of noncompliance with applicable health, safety, fire, and environmental requirements.

3. Treatment of Interest and Cost of Money

Under normal contracts awarded by Federal agencies, interest on borrowings is an unallowable cost (FAR 31.205-20, Interest and other financial costs), although contractors are entitled under FAR 31.205-10, Cost of money, to claim Facilities Capital Cost of Money (FCCOM) as a contract cost. (FCCOM is an imputed interest amount that is calculated by applying the Contract Disputes Act interest rate to the net book value of facilities assigned to a contract.) The profit or fee earned on contracts compensates the contractor for its cost of capital, which includes both interest on borrowings and return on equity.

Utility privatization contracts are unique instruments that combine real property transactions with the acquisition of utility services. The contracts may be up to 50 years in length, and require the contractor to invest its funds to acquire, renovate, replace, upgrade and/or expand the utility systems conveyed by the Military Department. The contractor investment costs for these efforts are usually amortized over the useful life of the systems in order to maintain a level funding profile for the Military Department. Because of the substantial time between when the costs are incurred and when they are charged to the military customer, the contractor will be permitted to recover its interest costs associated only with capital expenditures to acquire, renovate, replace, upgrade, and/or expand utility systems. This deviation to the FAR 31.205-20 is included in Appendix E. When the contractor is permitted to recover its interest costs, it will not be permitted to receive FCCOM as a contract cost. Interest rates used to calculate allowable interest costs must be limited to 600 basis points above the Contract Disputes

Act interest rate (41 U.S.C. 611) in effect at the time the contractor makes the capital expenditure. Contractors shall make a reasonable effort to obtain loans at competitive interest rates.

4. Cost Accounting Standards (CAS)

Title 48 Code of Federal Regulations Part 9903 requires CAS on all negotiated contracts in excess of \$500,000, except for:

- Sealed bid contracts;
- Contracts with small businesses;
- Contracts where the price is set by law or regulation;
- Contracts for the acquisition of commercial items;
- Contracts that are less than \$7.5 million if, at the time of contract award, the business unit of the contractor receiving the award is not performing any other contract subject to CAS.
- Contracts to be performed entirely outside the United States;
- Firm-fixed price contracts awarded on the basis of adequate price competition without the submission of cost or pricing data.

The military departments may grant waivers that meet the conditions in FAR 30.201-5(b). The military departments must submit each CAS waiver request to the Director, Defense Procurement, for review at least 14 days before granting the waiver. DoD contracting activities that are not within a military department must submit CAS waiver requests that meet the conditions in FAR 30.201-5(b) to the Director, Defense Procurement for approval at least 30 days before the anticipated contract award date. The specific requirements for the preparation, submission and approval of CAS waivers are at FAR 30.201-5.

Some Military installations are currently served by utility companies that may not be subject to the CAS. Requiring these companies to adhere to CAS may create significant costs to the company and discourage their participation in utilities privatization, which would limit competition and lead to a solution that is less than optimal. Defense Components should consider this potential limitation on competition in determining the need to request a CAS waiver. If the utility service price is not set by law or regulation, Components should consider using an appropriate index for determining future prices vice including price redetermination in the contract.

CONGRESSIONAL NOTIFICATION

The Secretary concerned must submit to the Defense Committees of Congress an economic analysis that meets the requirements of 10 U.S.C. 2688(e). In order to provide the Defense Committees with standardized notifications, the Military Department shall prepare congressional notification packages using the format at *Appendix D*. To ensure OSD is prepared to address questions from Congress, the Defense Components shall provide an advance copy of

notification packages to the USD(AT&L) two working days prior to notifying the committees. The Secretary concerned shall proceed with the conveyance of a utility system after a period of 21 days has elapsed from the date the committees receive the notification package unless one or more committees disapprove of the conveyance.

D. CONVEYANCE AND ACCESS

1. Conveyance

Because the intent of privatization is for the Department to get out of the utility business, the Defense Components shall convey all right, title, and interest in the utility system (as opposed to the underlying land) through appropriate conveyance documents. While leasing alone is not sufficient to transfer ownership, if the Secretary concerned determines that delayed transfer of title is economically preferable to an immediate transfer of title, the Secretary may structure the conveyance as a lease-purchase or a lease in furtherance of conveyance, as long as the non-federal entity at some point takes title to the asset.

The Military Departments must ensure that all transaction documents (e.g., the utility service contract and the real estate document that provides access to the utility system) vest them with sufficient rights to ensure continued services in the event of a default resulting in significant non-performance or abandonment. To that end, the Secretary concerned may include reversionary clauses to provide for title in the system to revert to the government in such extreme cases.

2. Access

The Military Department should provide the conveyee sufficient access to the utility system to perform all requirements of the utility service contract through an appropriate real estate document. The Military Department should convey the minimum interest in the underlying and surrounding real property necessary to provide reasonable access to, and use of, the conveyed utility system.

E. CONTRACT PERFORMANCE MONITORING

The Defense Components shall establish appropriate contract provisions and associated staffing (engineering and contracting) to ensure that the recipient of the utility system provides reliable service and manages and operates the utility system in a manner consistent with applicable federal, state and local regulations pertaining to health, safety, fire, and environmental requirements. To enhance the quality of service the contract provisions should incorporate contractual incentives and objective metrics that measure performance satisfaction.

The Defense Components shall monitor the service provider's execution of the contract regardless of the regulatory status of the service provider. The government's rights under the transactional documents shall be effectively utilized to ensure contract compliance. The contract should require a level of service equivalent to the level that would be obtained were all of the "should cost" items performed.